

INFORMATION

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DRAFT LEGISLATION ON PREFERRED SHARE FINANCING ISSUED

The Honourable Michael Wilson, Minister of Finance, today released draft legislation to implement the government's proposals relating to preferred share financing by corporations as well as explanatory notes elaborating on the provisions of the income tax reform draft legislation issued April 13.

The Minister noted that the draft legislation respecting preferred shares is based upon draft legislation tabled in the House of Commons on December 16, 1987 and takes into account constructive suggestions received since the proposals for taxation of preferred share dividends were released in June, 1987. These include the following changes:

- Proposed Part VI.1 of the Income Tax Act imposes a tax on dividends paid on preferred shares. A special higher rate of tax is levied under Part VI.1 where the share is retractable within five years of issue. As this higher rate of tax was announced on December 16, 1987, it will apply to shares issued after that date rather than after June 18, 1987.
- As first proposed, the preferred share financing amendments would have permitted a corporation to transfer its Part VI.1 tax liability to a subsidiary corporation to enable the subsidiary to claim an offsetting deduction against its corporate income tax. The present amendments permit the transfer to be made as well to any other related corporation.

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- Proposed Part IV.1 of the Act imposes a 10 per cent tax on dividends received by a financial institution on preferred shares issued before June 18, 1987 but acquired by the financial institution after that date. The draft Income Tax Regulations allow an exemption from the tax for dividends received on shares of a class listed on a prescribed stock exchange provided that the shares were acquired before December 16, 1987 and no more than 10 per cent of the shares are owned by the shareholder and non-arm's length persons. This exemption is extended to shares acquired after December 15, 1987, but only where the shareholding does not exceed 5 per cent. Similarly, dividends received by a financial institution on publicly-listed term preferred shares acquired after December 15, 1987 will qualify for the inter-corporate dividend deduction where there is no more than a 5 per cent shareholding.

Members of the public who wish to make suggestions for technical changes are asked to submit their representations as soon as possible and before May 20 at the latest, addressed to the Tax Policy - Legislation Division, Department of Finance, Ottawa, K1A 0G5.